WINTHROP WEALTH

APRIL 2021 CLIENT QUESTION OF THE MONTH: TAX-LOSS HARVESTING

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We are moving into Spring, which means (hopefully) warmer weather and that we are getting closer to Tax Day. The IRS recently announced that the tax filing due date for individuals was extended to May 17, 2021. IRS Commissioner Chuck Rettig commented that, "even with the new deadline, we urge taxpayers to consider filing as soon as possible." Individuals can also postpone federal income tax payments to May 17th without penalties and interest. Note that the deadline extension does not apply to estimated tax payments that are due on April 15, 2021 or state tax returns. Estimated payments are still due on April 15th and state filing and payment deadlines vary. Please consult with your tax professional with any specific questions regarding your tax returns.

Since we are approaching tax season, we thought it would be helpful to review the benefits of tax-loss harvesting. Tax-loss harvesting is achieved by selling an investment with a loss and immediately purchasing a different security with similar (but not identical) exposure. The key points are:

1. The loss on the sold security can be used to offset taxable gains. If there are losses in excess of any gains, up to $1,500 for an individual or $3,000 for married filing jointly can be used against ordinary income. Unused tax losses can be carried forward in perpetuity. The IRS rules on capital gains and losses can be found ***here***.
2. Since we simultaneously sell a security to capture a loss and purchase a different holding with similar exposure, the client is never out of the market. We can capture losses during declines, and as the market recovers the new position also recovers PLUS the client has a tax-loss to offset future gains.
    - Here is a simple example: Assume a client buys $10,000 worth of ABC security and one month later the price has declined by-15%. The client can sell the entire position of ABC for $8,500 and buy a similar (but not identical) position for the same amount, let's say the new position is XYZ holdings. Now assume that the value of XYZ holdings increases back to $10,000. The total value of the position is unchanged, but the client has a $1,500 tax loss to use against future gains.
    - Note, to ensure that investors do not sell a security to capture a loss and immediately buy it back, the IRS has implemented the "wash sale" rule. The rule states an investor cannot sell an investment at a loss and then buy a "substantially identical" security within 30 days before or after the sale.

We constantly look for opportunities to execute tax-loss harvesting trades. Typically, the best instances have occurred during significant market declines – the most recent examples are December 2018 and February/March 2020. As we've ***written about numerous times***, we know that the stock market has historically increased over long-term time periods, but that declines are quite common. The S&P 500 has averaged a peak-to-trough decline of-15.8% each year since 1928 despite producing a total annualized return of +9.6% over the same peri-od. In the latest example, the S&P 500 declined by nearly-34% from February 19, 2020 to March 23, 2020 before increasing by over +75% since then. When the inevitable market decline happens, we try to make lemonade out of lemons by tax-loss harvesting and rebalancing portfolios. These activities can provide significant benefits by capturing losses and/or reallocating to more attractive securities.

At Winthrop Wealth, we apply a total net worth approach to both comprehensive financial planning and investment management. Financial planning drives the investment strategy and provides a road-map to each client's unique goals and objectives. The comprehensive financial plan defines cash flow needs, is stress tested for various market environments, optimizes account structures, considers tax minimization strategies, and continuously evaluates financial risks as circumstances and/or goals change. The investment management process is designed to provide well-diversified portfolios constructed with a methodology based on prudent risk management, asset allocation, and security selection.

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Content in this material is for general information only and not intended to provide specific advice or recommendations for any individual.

The economic forecasts set forth in this material may not develop as predicted and there can be no guarantee that strategies promoted will be successful.

All indexes mentioned are unmanaged indexes which cannot be invested into directly. Unmanaged index returns do not reflect fees, expenses, or sales charges. Index performance is not indicative of the performance of any investment. Past performance is no guarantee of future results.

The Standard & Poor's 500 Index is a capitalization weighted index of 500 stocks designed to measure performance of the broad e market value of 500 stocks representing all major industries.

Financial planning is a tool intended to review your current financial situation, investment objectives and goals, and suggest potential planning ideas and concepts that may be of benefit. There is no guarantee that financial planning will help you reach your goals.

Likewise, it is important to remember that no investment strategy assures success or protects against loss. Asset allocation does not ensure a profit or protect against loss. There is no guarantee that a diversified portfolio will enhance overall returns or outperform a non-diversified portfolio. Diversification does not protect against market risk. All investing involves risk which you should be prepared to bear.

Rebalancing a portfolio may cause you to incur tax liabilities and/or transaction costs and does not assure a profit or protect against a loss.

This information is not intended to be a substitute for individualized tax advice. We suggest that you discuss your specific tax situation with a qualified tax advisor.